

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of Northern States
Power Company's Petition for
Approval to Merge with
Wisconsin Energy Corporation

FINDINGS OF FACT AND
CONCLUSIONS OF LAW

FLOW CONTROL AND COMPETITIVE EFFECTS

The "flow control" and "competitive effects" issues are three of five issues which were set for hearing by the Commission, as explained more fully below. This Report deals only with those two issues. Other Reports will deal with the other three issues.

The above-entitled matter came on for hearing before Allan W. Klein, Administrative Law Judge, on November 20, 1996, in St. Paul, Minnesota.

There were 22 formal parties to the proceeding as a whole. They are listed in the ALJ's Official Service List which is attached hereto as Attachment A. There were 11 parties who participated in this segment of the proceeding.

Appearances in this segment: David A. Lawrence, Attorney at Law, 414 Nicollet Mall, Minneapolis, Minnesota 55401, and Samuel L. Hanson and Michael C. Krikava, Briggs & Morgan, Attorneys at Law, 2400 IDS Center, Minneapolis, Minnesota 55401, appeared on behalf of Northern States Power Company ("NSP"); Gregory Huwe and Brent L. Vanderlinden, Assistant Attorneys General, NCL Tower, Suite 1200, 445 Minnesota Street, St. Paul, Minnesota 55101, appeared on behalf of the Department of Public Service ("DPS" or "Department"); and Eric F. Swanson, Eric Peck and Carol Bennett, Assistant Attorneys General, NCL Tower, Suite 1200, 445 Minnesota Street, St. Paul, Minnesota 55101, appeared on behalf of the Attorney General's Office Antitrust and RUD Divisions ("OAG"). Jay Quam, Fredrikson & Byron, Attorneys at Law, 1100 International Centre, 900 Second Avenue South, Minneapolis, Minnesota 55402, appeared on behalf of Cooperative Power Association ("CPA"); Lee Cullen, Cullen, Westin, Pines & Bach, Attorneys at Law, 20 North Carroll Street, Madison, Wisconsin 53703, appeared on behalf of Wisconsin Intervenors ("WI") (a coalition consisting of Madison Gas & Electric Company, the Wisconsin Federation of Cooperatives, and the Citizen's Utility Board of Wisconsin); and Susan Hedman, 203 North LaSalle Street, #1390, Chicago, Illinois 60601

appeared on behalf of the Environmental Coalition ("EC") (Izaak Walton League of America, Minnesotans for an Energy Efficient Economy, and the Environmental Law and Policy Center of the Midwest). Pam Marshall, 1916 Second Avenue South, Minneapolis, Minnesota 55403, appeared on behalf of Energy CENTS Coalition ("ECC"). Louis Sickmann, Betsy Engelking and Clark Kaml, Suite 350, Metro Square, 121 Seventh Place East, St. Paul, Minnesota 55101, appeared in a neutral capacity on behalf of the Minnesota Public Utilities Commission.

NOTICE

Notice is hereby given that, pursuant to Minn. Stat. § 14.61, and the Rules of Practice of the Public Utilities Commission and the Office of Administrative Hearings, exceptions to this Report, if any, by any party adversely affected must be filed within 20 days of the mailing date hereof with the Executive Secretary, Minnesota Public Utilities Commission, 350 Metro Square, 121 Seventh Place East, St. Paul, Minnesota 55101. Exceptions must be specific and stated and numbered separately. Proposed Findings of Fact, Conclusions and Order should be included, and copies thereof shall be served upon all parties. If desired, a reply to exceptions may be filed and served within ten days after the service of the exceptions to which reply is made. Oral argument before a majority of the Commission will be permitted to all parties adversely affected by the Administrative Law Judge's recommendation who request such argument. Such request must accompany the filed exceptions or reply, and an original and 14 copies of each document should be filed with the Commission. The Commission may, by Order, vary the deadline set forth above. Due to the unusual format for the issuance of the Reports in this matter, parties are urged to contact the Commission to ascertain the appropriate schedule for filings.

The Minnesota Public Utilities Commission will make the final determination of the matter after the expiration of the period for filing exceptions as set forth above, or after oral argument, if such is requested and had in the matter.

Further notice is hereby given that the Commission may, at its own discretion, accept or reject the Administrative Law Judge's recommendation and that said recommendation has no legal effect unless expressly adopted by the Commission as its final order.

STATEMENT OF ISSUES

1. To what extent will it be feasible for Primergy to use its transmission ownership and control of the MAPP-WUMS interface to restrict the flow of non-Primergy sales over its wires?

2. What, if any, is the impact of such a restriction on Minnesota utilities other than Primergy?

Based upon all of the files and proceedings herein, the Administrative Law Judge makes the following:

FINDINGS OF FACT

Procedural Background

1. On or about May 1, 1995, NSP and WEC announced their intent to merge.

2. The merged entity is to be known as Primergy Corporation, which is to be the parent company of both NSP and WEC and registered under the Public Utility Holding Company Act of 1935.

3. On August 4, 1995, Northern States Power Company filed with the Commission its petition for approval of a merger with Wisconsin Energy Corporation ("WEC" or "WEPCO") in the above-captioned matter. As part of its filing, NSP also requested Commission approval to acquire certain gas properties of NSP-Wisconsin, to defer accounting on its merger expenses, and to reduce retail electric rates by 1.5 percent across the board and freeze them for four years.

4. Pursuant to Commission notice, interested parties filed initial comments and petitions to intervene by January 15, 1996. Following responsive comments, the Commission invited additional comments by April 2, 1996, addressing such procedural issues as the identification of any material factual disputes which would require a contested case hearing and the proposed scope of any hearing.

5. On June 6, the Commission met to consider this matter, and on June 25, 1996, issued its Order Establishing Procedural Framework and Notice and Order for Hearing ("Order"). The Commission distilled the numerous issues raised by the parties into three separate groups. One group was identified as having been adequately presented in prior filings, so that the Commission felt it had an adequate record to resolve those issues without any additional evidence. The second group was one where the Commission desired additional filings, but did not believe a contested case was needed. Finally, the third group consisted of several issues raised in connection with the petition which the Commission decided to refer for a contested case proceeding before the Office of Administrative Hearings. The issues referred for contested case hearing were:

- * what are the expected Minnesota jurisdictional merger-related net savings by year for ten years following the merger?
- * what are the appropriate characteristics of an electric rate freeze (e.g. exceptions, duration, etc.) in these circumstances?

- * what is NSP's pre-merger revenue requirement based on a 1996 test year adjusted for known pre-merger changes in 1997?
- * to what extent will it be feasible for Primergy to use its transmission ownership and control of the MAPP-WUMS interface to restrict the flow of non-Primergy sales over its wires?
- * what, if any, is the impact of such a restriction on Minnesota utilities other than Primergy?

6. Following a prehearing conference held on July 10, interested parties filed proposals for schedules, and Judge Klein issued a Prehearing Order on August 5. This Order established the hearing schedule and procedural guidelines governing the conduct of the contested case proceeding. The Prehearing Order also allowed for informal public hearings on dates and at locations to be determined. Public hearings were held as follows:

<u>Date</u>	<u>Time</u>	<u>Location</u>
October 30, 1996	7:00 P.M.	Nisswa, Minnesota
November 4, 1996	7:00 P.M.	Mankato, Minnesota
November 15, 1996	1:00 P.M.	Minneapolis, Minnesota

7. The Prehearing Order also scheduled formal evidentiary hearings divided into three segments as follows:

<u>Segment</u>	<u>Dates</u>	<u>Judge</u>
Flow Control & Competitive Effects	November 18-21	Klein
Merger Savings & Freeze Conditions	November 22-27	Giles
Pre-Merger Revenue Requirement	December 2-6	Luis

Prehearing administrative activities and procedural matters not particularly related to any specific issues were handled by Judge Klein.

Public Hearings and Comments

8. Public comments, both at the public hearings and in writing, generally opposed the merger. There were, however, comments from members of Minnesota Utility Investors and from some civic leaders who had worked with NSP in various community projects, which supported NSP in its desire for a merger.

9. Those opposed to the merger mentioned topics such as environmental degradation due to increased operations of coal plants in order to sell electricity to other

states; loss of regulatory control to Washington and inability to impose Minnesota values in areas such as conservation, renewables, and pollution; long-term financial impacts on low-income persons once the freeze ended; loss of local jobs and diminished responsiveness to customer needs for service; fears that municipal and rural cooperatives would no longer be able to compete with Primergy because of rates and control of the grid; horizontal market power ("anti-bigness"); and a number of other issues, the vast majority of which did not relate to the five issues set for hearing by the Commission. The Administrative Law Judge urged members of the public to write directly to the Commission in order to voice their concerns about issues beyond the five which had been set for hearing. However, a number of commentators did take the opportunity of the public hearings and letters to the ALJs to express their concerns as noted above. Of the five issues set for contested case hearing, the only one which drew much comment was the proposed rate reduction and freeze, which a number of individuals characterized as too small and too short. Several comments from businesses, however, characterized the reduction and freeze as meaningful and urged that it be adopted promptly.

10. At each of the hearings, a representative of Minnesota Utility Investors expressed that organization's support for the merger. They cited lower rates, pending deregulation on a national scale, and the need to allow NSP the flexibility to position itself for this change. While they welcomed prospects of a rate reduction and a rate freeze, they urged that NSP be given some flexibility to deviate from the freeze in the event of outside influences, such as unknown governmental actions.

Prehearing Motions

11. On September 16, 1996, the Environmental Coalition and the Citizens' Utility Board filed a Motion to Stay Proceedings. The motion sought a stay until there was a resolution of the issues arising from the allegations of improper ex parte contact between NSP and members of the Commission. Following a comment period, on October 1, 1996, the Administrative Law Judge entered his Order Denying Stay of Proceedings.

12. On October 3, 1996, Otter Tail Power Company, the Minnesota Office of Attorney General - Antitrust and RUD Divisions, the Citizens' Utility Board, the Environmental Law and Policy Center, Madison Gas & Electric Company, and the Wisconsin Electric Cooperative Association filed a Motion to Allow the Introduction of Relevant Portions of the FERC Record. Following an expedited comment period, the Administrative Law Judge issued a Memorandum on October 17, indicating that the Motion would be granted subject to certain conditions designed to restrict the scope of the hearing to the issues identified by the Minnesota Commission in its June 25 Order. The decision was memorialized within the ALJ's Order on Prehearing Motions dated November 25, 1996. The FERC hearing material is in the record as Joint Ex. 1.

13. On October 24, Northern States Power Company filed a Motion to Strike Certain Intervenor Testimony. Following an expedited comment period, the

Administrative Law Judge issued a Memorandum on November 7, indicating that the Motion would be granted in its entirety. The decision was memorialized within the ALJ's Order on Prehearing Motions dated November 25, 1996. The stricken testimony, which had been filed by the Environmental Coalition and the Energy CENTS Coalition, dealt with environmental and low-income issues which the Commission had determined would not be a part of the contested case hearing. The stricken testimony was offered as an Offer of Proof at the start of the evidentiary hearing. EC/ECC Exs. 1-4.

14. On October 31, Wisconsin Intervenors filed a Motion to Introduce Record of the Public Service Commission of Wisconsin. Following an expedited comment period, a Memorandum was issued on November 7, granting the Motion in part, and denying it in part. The distinction was drawn in order to restrict the record to that material which was relevant to one of the five issues referred for hearing in the Commission's June 25 Order. The decision was memorialized within the ALJ's Order on Prehearing Motions dated November 25, 1996. The Wisconsin hearing material is in the record as Joint Ex. 2.

15. On November 13, Commonwealth Edison Company filed a Motion to Intervene Out of Time. After allowing the parties to comment on the motion at the start of the evidentiary hearing, the Administrative Law Judge granted the motion, but limited ComEd's participation to the filing of briefs. Tr. 2, p. 39.

16. On November 19, 1996, the Environmental Coalition, Energy CENTS Coalition and the Citizens' Utility Board filed a Motion for Stay of Proceedings, asking that the impending hearing be stayed while the Commission considered a parallel Petition for Reconsideration in connection with the ex parte contact issue.^[1] On November 20, at the commencement of the evidentiary hearing on the flow control and competitive effect issues, parties were given an opportunity to present argument on the Motion for a stay. The Administrative Law Judge then ruled that the Motion would be denied and the hearing would go forward, but that he would grant the request for certification to the Commission. Tr. 1, pp. 33-34. This was memorialized in an Order Denying Stay and Certifying Petition to Commission dated December 3.

Flow Control and Competitive Effects

Background

17. The hearing on the flow control and competitive effects issues was conducted on November 20 and 21. Six parties submitted testimony on the competitive impacts issues: NSP; the Office of the Attorney General, participating through both its Residential and Small Business Utilities Division and its Antitrust Division; the Department of Public Service; the Wisconsin Intervenors, comprised of Citizens' Utility Board, Madison Gas & Electric Company and Wisconsin Federation of Cooperatives; the Environmental Coalition, comprised of the Izaak Walton League of America,

Minnesotans for an Energy Efficient Economy and the Environmental Law and Policy Center of the Midwest; and the Energy CENTS Coalition. In addition to the parties filing testimony in this phase of the hearing, Cooperative Power Association ("CPA") also participated in the hearings. All parties filed post-hearing briefs, with EC joining in the brief of WI.

18. NSP currently serves customers in Minnesota, North and South Dakota, Wisconsin and the Upper Peninsula of Michigan. It owns and operates more than 6800 megawatts (MW) of generating capacity and, in 1994, it relied on that generating capacity and power purchases to cover a peak load of 7101 MW. NSP also has capacity rights to over three-fourths of the firm transfer capability from Manitoba to the U.S. Joint Ex. 1 at Ex. CI-1, pp. 28-29.

19. NSP is the largest utility in the Mid-continent Area Power Pool (MAPP). MAPP is one of the Regional Reliability Councils of the North American Electric Reliability Council (NERC). The region covered by MAPP extends from western Wisconsin to all of Minnesota, North and South Dakota, Nebraska, Iowa, and portions of Canada.

20. As a subsidiary of Primergy, NSP would provide both electricity and gas in Minnesota, and North and South Dakota, and would provide gas in Wisconsin.

21. WEPCO is presently a subsidiary of Wisconsin Energy Corporation (WEC), a Wisconsin energy holding company. WEPCO serves customers in southeastern, east central, and northern Wisconsin, and in the Upper Peninsula of Michigan. WEPCO owns approximately 5700 MW of generating capacity and 1653 miles of transmission lines of 67 kilovolts (kV) and above. In 1995, WEPCO had a peak load of 5225 MW.

22. WEPCO is a member of the Mid-America Interconnected Network (MAIN), another of NERC's nine regional councils. The region covered by MAIN encompasses the Upper Peninsula of Michigan, all of Wisconsin and Illinois, and the eastern half of Missouri.

23. Wisconsin Energy, the Primergy subsidiary formed from the merger of WEPCO with NSP-W (NSP's present Wisconsin subsidiary), would provide electricity and gas in Wisconsin and the Upper Peninsula of Michigan.

24. WEPCO is the largest utility in WUMS (the Wisconsin and Upper Peninsula of Michigan System area). WUMS includes five other electric utilities in Wisconsin and the Upper Peninsula of Michigan. WUMS is bordered on the north by Lake Superior and on the east by Lake Michigan. Only two routes exist to and from which energy can be transmitted into or from the WUMS market -- south and west.

25. To the south, WUMS is bordered by Commonwealth Edison (CE), forming the Northern Illinois (NI)/WUMS interface. WEPCO owns two of the three 345

kV lines between WUMS and Illinois to the south. On the southern side of the NI/WUMS interface, CE controls 100% of the transfer capability across the interface.

26. MAIN has projected a total transfer capability of about 1000 MW during the summer of 2001.

The MAPP-WUMS Interface

27. On the west, WUMS is bordered by MAPP and obtains power through the MAPP-WUMS interface. By formal agreement, WEPCO shares the available transfer capacity on the eastern or WUMS side of the MAPP-WUMS interface with two other parties. WEPCO controls 52% of the capacity, Wisconsin Power & Light (WP&L) controls 28%, and WPSC controls the remaining 20%.

28. On the western or MAPP side, NSP has the right to nearly all of the transmission capacity over the interface.

29. The MAPP-WUMS interface consists of the transmission lines and other facilities that provide an interconnection for power flowing from Minnesota to Wisconsin. The interface is physically located in wholly Wisconsin, but its capacity is affected by actions taken throughout the MAPP and MAIN areas. NSP and Dairyland Power Cooperative ("DL") are the MAPP utilities that own the transmission facilities on the west side of the interface. WEC, Wisconsin Public Service ("WPS") and Wisconsin Power and Light ("WPL") are the MAIN utilities that own the transmission facilities on the east side of the interface. NSP Ex. 16 at 3-4.

30. The interface consists of a number of transmission lines. NSP and WEC own the principal line between the two areas, the 345-kV line connecting the substations of King-Eau Claire-Arpin-Rocky Run and North Appleton. However, WPL and WPS own the Arpin substation and the Rocky Run substation, respectively. NSP and WPS own the 115-kV line connecting the substations of King-Pine Lake-Hydro Lane-T Corners-Wein-Cassel-Sherman Street. DL and WPL own a 161-kV interconnection at Nelson Dewey. Finally, DL and WPL own several 69-kV interconnections. NSP Ex. 16 at 4. A graphic portrayal of these lines is contained in Joint Ex. 1, Ex. CI-36, which is a map prepared by MAPP that illustrates the location of these lines, substations and generators.

31. The MAPP-WUMS interface has a total capacity of 700 MW^[2] for long-term planning purposes. However, 700 MW is neither the maximum nor minimum transfer capability of the interface at any given time. The 700-MW limit applies to certain peak hours only. While under some extreme conditions, the transfer capability may be lower than 700 MW, there are many hours during the year in which transfer capability substantially exceeds 700 MW. NSP Ex. 16 at 8-9; DPS Ex. 19 at 3. There are plans to upgrade the MAPP-WUMS interface to 1200 MW of firm transfer capability for long-term planning purposes, by the year 2001 or 2002.

Problems Created by the Constrained Interface

32. The practical implication of the limited capacity of the interface is that there are times when there is a desire to pass more power through it than it can safely handle. Which power is allowed through, and which is denied access, will affect the profit and loss statement of those who desire to use the interface. The general fear expressed by WI is that Primergy will use its ownership and control of the interface to benefit itself and harm its competitors.

33. Some idea of the frequency of the capacity constriction on the interface can be gained from an examination of recent line loading relief incidents. Line loading relief (LLR) is a procedure developed to maintain the reliability of a transmission network. It is a process whereby energy transfers are reduced to a level which the transmission network can reliably support and maintain securely in order to avoid end-use customer service outages. When transmission system loading reaches a point where loss of one facility either causes or could cause an overload or an instability condition of the network, line loading relief is requested. In the case of MAPP, a transmission line operator, such as NSP, would notify MAPP that a certain line was carrying power at or near its limit. The MAPP Coordination Center would then request energy transaction information from its members in order to determine who is using the line and what kind of transactions are involved. The MAPP Coordination Center then determines the impact that each energy transaction has on the facility under stress and the MAPP Coordination Center would then order energy transactions curtailed, based on priority and impact on the facility at risk. Firm transactions have priority over non-firm transactions. NSP Ex. 12, at pp. 3-5.

34. Logs are kept of these line loading relief incidents, and are in the Minnesota record. Joint Ex. 2, Ex. 98, is a complaint from Wisconsin Public Power, Inc. regarding constraints over the interface. Attached to it is a log of line loading relief incidents from January 7, 1996 through October 23, 1996. The complaint of Wisconsin Public Power, Inc. provided, in part, as follows:

This fall [the fall of 1996], WPPI and other Eastern Wisconsin utilities are continuing to have their imports of energy from the west interrupted on an almost daily basis. This is unprecedented and reflects a major change in the availability of the Wisconsin interface for the benefit of Wisconsin customers. Enclosed is an updated log of MAPP line loading relief requests made from January 1, 1996 through October 22, 1996. These interruptions are continuing to occur on a regular basis during all hours of the day and night!

A slightly different time period was analyzed by WI Witness Russell. He confirmed that there were numerous calls for relief and actual curtailments during the period January 1 through September 22, 1996. During this period of time, there were 207 calls for relief, and 116 curtailments. While those absolute numbers do not mean

much without more data, they do support the allegations raised by WPPI. WI Ex. 5, Attach. WAR-4.

35. WI has catalogued the methods whereby, as a result of Primergy's direct operational control over the MAPP-WUMS Interface, WI fears that Primergy could reduce or alter transfer capacity. WI contends that, with respect to the transmission system, Primergy could:

- not implement diligently or promptly various operating guides designed to maintain or increase capacity;
- implement other distribution operating guides so as to reduce bulk transfer capacity;
- develop and invoke new operating guides applicable to competitors;
- delay or defer certain upgrades or improvements to the system;
- change the number and location of devices which provide voltage support;
- alter input data determining permissible voltage drops;
- vary hourly load forecasts at specific interconnections;
- call for line-loading relief or its successor within MAPP or MAIN;
- schedule repairs for transformers and other transmission equipment in a way which benefits itself or harms its competitors.

WI contends that Primergy could also take the following generation actions:

- change the pattern of dispatch of key power plants so as to reduce voltage support and reduce transfer capacity;
- take key generation facilities off-line for maintenance in a way which reduces transmission capacity;
- retire strategically located plants early when regional transfer needs would indicate otherwise;
- schedule a pattern of purchase, sale and/or resale so as to adversely affect transfer capacity.

36. WI contends that Primergy could also reduce perceived or planned transfer capacity, as follows:

- employ different ratings for lines and other equipment depending upon the desired outcome;
- model different loads and use different load forecasts to suit its purpose;
- develop and propose low-cost upgrades for its own needs, and more expensive improvements for its competitors;
- control input data for various regulatory planning studies;
- delay the filing and prosecution of applications for new transmission.

37. These concerns were litigated before FERC Administrative Law Judge Michel Levant during a six-day hearing in June of 1996, and again before Wisconsin PSC Hearing Examiner Donna Paske in an equally lengthy proceeding in early November of 1996. The FERC record is a part of the Minnesota record, labeled as Joint Ex. 1. The relevant portions of the Wisconsin record are in the Minnesota record, labeled as Joint Ex. 2. As of the time of this writing, neither FERC nor Wisconsin have issued Final Orders. While there is no Hearing Examiner's Report from the Wisconsin proceeding, there is a 95-page, single spaced Initial Decision from ALJ Levant in the FERC proceeding. In response to the concerns raised by WI in that proceeding,^[3] Judge Levant concluded:

Staff and CI's litany of ways in which Primergy would allegedly manipulate transfer capability over the MAPP/WUMS interface, as well as the MAIN/WUMS interface, rest upon unsupported speculation as to Primergy's likely conduct. Indeed, some of the enumerated actions would involve illegal activity, fraud, deliberate violations of Commission [FERC] regulations and NERC policies, and a variety of other questionable actions. It is notable that none of these manipulative acts attributed to Primergy are shown to result specifically from the merger, but rather are actions that could be taken at any time by NSP, WEPCO, or by any other utility, quite apart from the merger. Nor is there probative evidence in the record that NSP or WEPCO have ever acted in this manner in the past or would be likely to do so in the future.

* * *

CI's and Staff's far reaching speculative scenarios based on improper and illegal actions cannot form the basis for anticipating

the likely outcomes of the merger and should not be given significant weight in determining whether Primergy would have the ability or the incentive to negatively impact competition by manipulating transfer capacity.

* * *

Accordingly, it is found that the merger will not provide Primergy with the ability or the incentive to negatively impact competition through manipulation of transfer capacity through constrained interfaces or by altering the availability, reliability, or price, of transmission service.

Presiding Administrative Law Judge's Initial Decision, issued August 29, 1996, at pages 48, 49 and 51, respectively.

38. A slightly different problem caused by the constrained interface occurred in 1993. Madison Gas & Electric requested transmission service for two months (its peak summer months) in each of the years 1996 to 2000 (Joint Ex. 1, Ex. CI-30). It sent a letter to WEPCO, asking for wheeling of 40 megawatts of capacity from Dairyland to MG&E during the months of July and August. WEPCO responded by indicating that it would make firm transmission service available so long as it had adequate capacity to do so, but pointed out:

Your request is for transmission service commencing in 1996 and extending through 2000, over a critical interconnection for a two-month period (July, August), during which time the system peak demands normally occur. As you know, the firm capability of the WUMS-Minnesota interface is limited at the present time. Granting your request would tie up a portion of that limited capability for the two-month period of the year when our peak loads occur and when usage of the interface may be great. In the recent past, heavy use has been made of the interface facilities and such use is projected to continue throughout the time period covered by your request.

In a follow-up letter to MG&E, a different WEPCO official indicated that granting the request for 40 megawatts of transmission service for only those two peak months would:

. . . severely diminish the value of that block of transmission capability for the remaining ten months of the year Thus, to the extent your firm transmission service for two months prevented Wisconsin Electric from using or selling that transmission capability for a longer period of time, the company would lose the revenues associated with such alternate transactions In the alternative, if MG&E wishes Wisconsin Electric to commit presently to reserving

40 megawatts of firm transmission capacity, the company is willing to do so if MG&E purchases such capacity on a long-term basis, that is, for the full 12 months of each year involved.

Judge Michel Levant found "WEPCO legitimately exercised its right to refuse this request for the reason that it would have inappropriately tied up scarce firm transmission capacity throughout the year with MG&E paying for only two months". Initial Decision, at p. 48-49. The undersigned Administrative Law Judge agrees with Judge Levant. Moreover, this incident occurred in 1993, well before the merger was announced. The merger would not affect the odds of its reoccurrence.

39. Nothing has been presented in the Minnesota hearing which would lead to contrary findings or conclusions from those of Judge Levant cited in Findings 37 and 38 above. This is because the cumulative effect of a number of mitigative factors has removed or blocked Primergy's motivation and ability to restrict the transfer of non-Primergy energy over the interface.

Safeguards Against Abuse

40. Primergy would be unlikely to manipulate the system or engage in anti-competitive practices if such practices were unlikely to result in significant monetary gain. In the absence of significant potential gains, Primergy's incentive to engage in anti-competitive practices would be minimal. The main factors that would reduce Primergy's incentive to manipulate the interface are the special commitments made by Primergy in connection with its merger proposal. In addition to those economic commitments, there are institutional factors which will make it very difficult for Primergy to manipulate the interface without getting caught. Both the economic commitments and the institutional barriers will be addressed in detail below.

41. The special commitments that Primergy (specifically the operating utilities of NSP and WEC) has agreed to are: 1) selling economy energy at WEC's incremental cost when the interface is constrained; 2) waiving its native-load priority for economy transactions over the interface; and 3) upgrading the MAPP-WUMS interface.

42. First, when the interface is constrained, Primergy has agreed to price WEC's economy sales to any member of WUMS at WEC's incremental energy cost plus the posted transmission rate. NSP Ex. 8 at 10-13. If Primergy deliberately constrained the interface, it might forego transmission revenues that it could have received from energy sales of other MAPP members to WUMS members. Additionally, Primergy might lose revenues from NSP's foregone energy sales to WUMS. Of course, Primergy could also receive revenues from WEC's additional energy sales to WUMS. However, because of Primergy's commitment to sell energy at WEC's incremental cost, Primergy would be unable to realize any excessive profits on these sales; rather, Primergy would receive only normal economic profits on these sales. Absent Primergy's ability to earn excessive profits by deliberately constraining the interface, it would have no economic

incentive to do so. In fact, such an action might reduce Primergy's profits. DPS Ex. 19 at 5-6.

43. Second, Primergy has agreed to waive its native-load priority for economy transactions. NSP Ex. 8 at 13-14. Under existing FERC policies, economy-energy transactions between NSP and WEC would be considered native-load transactions. Therefore, when the interface was constrained, such transactions would be entitled to a higher priority than a third party's economy-energy transactions. However, Primergy has agreed to waive this native-load priority for no longer than six years following the merger, or until the interface is expanded, whichever occurs first. NSP Ex. 8 at 14.

44. As a result of this commitment, post-merger economy-energy transfers between NSP and WEC would have the same level of priority as they had before the merger. Therefore, a deliberate attempt by Primergy to constrain the interface might force Primergy to forego transactions that are the most profitable. When the interface was constrained, MAPP (not Primergy) would determine the priority of various economy transactions. Therefore, other utilities' economy transactions may be scheduled ahead of Primergy's, thus eliminating potential sales for Primergy. DPS Ex. 19 at 6-7.

45. Third, Primergy has committed, as part of the merger, to proceed with its "Phase I" and "Phase II" transmission projects. Phase I is known as the Baldwin-Marathon City Project. This is a joint project of NSP and WPS. NSP and WPS filed for a Certificate of Public Convenience with the PSCW on September 15, 1993. The PSCW scheduled a hearing on the project to begin in 1996. Completion of the project is expected by 2001. NSP Ex. 16 at 6. After completion of the Phase I project, the MAPP-WUMS interface will have a transfer capability of 900 MW. NSP Ex. 16 at 8.

46. Phase II is a joint project of NSP and DL to construct a new, 230-kV line from NSP's Chisago County (Minnesota) substation into Western Wisconsin. Construction applications have been filed with the PSCW, the Minnesota Environmental Quality Board and the Rural Utilities Service in September 1996. Completion of the project is expected sometime in 2002. NSP Ex. 16 at 10. After completion of the Phase II project, the MAPP-WUMS interface will have a transfer capability of 1,200 MW. NSP Ex. 16 at 8.

47. In addition to these upgrades, in Wisconsin Advanced Plan 6 ("AP6"), the PSCW approved up to 1,200 MW of MAPP-WUMS transfer capability and allowed the utilities involved in the potential upgrade projects one year to file a construction application. As a result, an Interface Collaborative Group ("Group") was formed to obtain consensus on a plan for submitting a construction application to the PSCW. The Group continues to meet on a regular basis to discuss transmission-related issues. In July 1996, the Group completed a study that identifies facilities limiting MAPP-WUMS transfers prior to the completion of the Phase I and Phase II projects. The Group has also identified four short-term projects that may take no more than a year to complete.

Upon completion of these projects, the transfer capability of the MAPP-WUMS interface will increase by as much as 300 MW in 1997. NSP Ex. 16 at 12; NSP Ex. 17 at 3.

48. NSP is now committed to completion of these near-term interface projects. Engineering and design is progressing and some equipment has been ordered. NSP is targeting June 1, 1997 as a completion date. NSP Ex. 17 at 10.

49. Thus, short-term upgrades planned to be completed in 1997 will significantly improve transfer capability. The completion of Phase I would further significantly reduce the constraints on the interface. The completion of Phase II would probably completely eliminate the constraints on transfer capability. Absent effective constraints on the transfer capability of the interface, Primergy would have no economic incentive to manipulate it. DPS Ex. 19 at 9.

50. Primergy's ability to manipulate the interface is further restricted by certain institutional factors, which include FERC Orders 888 and 889, the recently-approved MAPP Restated Agreement, and the requirement that there be an Independent System Operator ("ISO"). Each of these will be described below.

51. The purpose of FERC Order Nos. 888 and 889 is to provide open and equal transmission access in order to accommodate increased competition in the wholesale electricity markets. Many of the provisions in these Orders are aimed at preventing anti-competitive behavior by transmission-owning utilities. Some of the main requirements of Order No. 888 are as follows.

52. First, all utilities that own, operate or control interstate transmission facilities must file tariffs that offer others the same transmission services they provide themselves under comparable terms and conditions. NSP Ex. 16 at 5.

53. Second, for all utilities that own, operate or control interstate transmission facilities the Order establishes:

- priorities for obtaining Firm Point-to-Point services,
- reservation priorities for Non-Firm services,
- rules governing the reservation of transmission capacity, and
- curtailment provisions.

DPS Ex. 19 at 11-12.

54. Several provisions of Order No. 889 also prevent anti-competitive behavior. The first provision is the Open Access Same-Time Information System ("OASIS") rule. NSP Ex. 16 at 5. This rule requires transmission providers to establish or participate in an OASIS that meets certain requirements. Under this provision,

Primergy would have to establish a real-time information network. This information network must provide real-time information about transmission availability, scheduling, economic dispatch, service interruptions and system reliability. This information must be posted on an electronic bulletin board and be made available to others. DPS Ex. 19 at 12.

55. The second provision of Order 889 establishes standards of conduct. These standards of conduct are designed to prevent employees of public utilities engaged in marketing functions from obtaining preferential access to information about the transmission system or from engaging in unduly discriminatory business practices. The standards of conduct also require utilities to separate their transmission operations/reliability functions from their marketing/merchant functions. Finally, the standards prevent operators of transmission systems from providing marketing employees and employees of affiliates with transmission-related information not available to all customers at the same time through public posting on the OASIS Electronic Bulletin Board. DPS Ex. 19 at 12-13. Under the OASIS information system provided for in Order No. 889, all users of the transmission system would receive, on a real time basis, information regarding transmission conditions and thereby would be in a position to learn of any attempts by Primergy to deliberately manipulate the transmission system. Moreover, any violations of the ISO system would be subject to an enforcement mechanism that would be established for the ISO, as well as to continuing FERC jurisdiction.

56. The MAPP Restated Agreement was approved by FERC on September 12, 1996. The Agreement expands membership in the power pool, creates a Regional Transmission Group ("RTG") that meets FERC's requirements, and promotes open-access transmission. Below is a summary of the main features of the Agreement.

The Agreement incorporates into MAPP an RTG which:

- provides for the comparable and efficient provision of transmission service within and contiguous to the MAPP region;
- furthers the benefits of coordinated regional transmission planning;
- resolves disputes over the provision of transmission service; and
- establishes a power and energy market to obtain the benefits of the efficient voluntary purchase and sale of electric capacity and energy at competitive rates.

57. MAPP membership is open, without geographic limitations, to:

- any electric utility, defined as any entity, person, federal agency (including any federal power marketing agency and the Tennessee Valley Authority) or state agency (including any municipality) that sells electric energy;
- any transmitting utility, defined as any electric utility, qualifying cogeneration facility as defined in the Federal Power Act, qualifying small power production facility as defined in the FPA, or other entity which owns, operates, or has rights equal to ownership in electric power transmission facilities used for the transmission of electric energy for sale at wholesale; and
- any other entity generating electric energy for sale for resale.

DPS Ex. 19 at 16.

58. The Agreement allows small entities to participate as joint members. Regulatory agencies with authority in the MAPP region may also become regulatory participants entitled to receive notice of meetings and to participate in meetings, but not to vote.

59. MAPP has been structured under the Agreement to include a Management Committee, Executive Committee, Reliability Council, Regional Reliability Committee, Power and Energy Market Committee, Alternate Dispute Resolution Committee, and Regional Transmission Committee. The Regional Transmission Committee is MAPP's RTG. This committee reviews tariffs for conformity with the Agreement and sets standards and requirements for the use of the MAPP transmission grid. DPS Ex. 19 at 17.

60. The Agreement conforms to FERC's RTG Policy Statement because it provides for:

- broad membership over a broad geographic area;
- consultation and coordination with state authorities;
- an obligation to provide transmission service;
- coordinated transmission planning;
- fair and non-discriminatory governance and decision-making;
- voluntary dispute resolution procedures, and
- exit provisions.

61. Under FERC Order No. 888, MAPP will have to file an equal open-access pro forma transmission tariff no later than December 31, 1996. DPS Ex. 19 at 18.

62. The Agreement also directly affects the control of the MAPP-WUMS interface. The main concern regarding the interface is Primergy's ability to constrain interface access for its own benefit. Under the Agreement, MAPP's RTG will determine the LLRP and will set transaction priorities when the interface is constrained. Therefore, if Primergy deliberately constrained the interface, the final outcome would be dictated by the RTG's dispatch center. This outcome might actually hurt (rather than benefit) Primergy. Additionally, the RTG will have a dispute resolution procedure. This procedure ensures that MAPP's members will not abuse their transmission tariffs, schedules or plans. The dispute resolution procedure will also deal with complaints that a transmission tariff, schedule, or plan is unduly discriminatory as applied to the member, imposes undue or unreasonable costs or other burdens on the member, or is otherwise contrary to the terms of the Agreement or applicable requirements of state or federal law. DPS Ex. 19 at 18-19.

63. Finally, and perhaps most importantly, Primergy has agreed to the creation of an ISO. In general, an ISO would have responsibility for operation of the transmission facilities of ISO members, including the filing and administration of transmission tariffs and the scheduling of all transactions. An ISO would be a utility subject to the jurisdiction of the Federal Energy Regulatory Commission under the Federal Power Act. In Order 888, the FERC set out several standards for ISO design that it would favor, and the FERC has begun making case-by-case decisions on individual ISO proposals.

64. In this and other pending merger cases, Primergy utilities have committed to assisting in the formation of an ISO and to becoming a member. FERC Law Judge Levant recommended that an ISO be formed as a condition of FERC approval of the Primergy merger, and there is no reason to believe that it will not be part of the FERC's final Order. On October 9, 1996, Primergy utilities submitted to the FERC a Unilateral Settlement Offer, consisting of Applicants' proposed ISO bylaws and form of contract between the ISO and transmission owner-members, designed to meet FERC ISO guidelines and Judge Levant's recommendations.

65. An ISO will be most effective in insuring efficient transmission system operations and maximizing regional transmission use through regional transmission tariffs if the ISO has broad membership. Since utilities generally cannot be compelled to join an ISO, it is important that regulation not impose unnecessary conditions which discourage broad ISO participation. This is an important point that can get lost in the myriad of details over how an ISO should be structured and operated -- a primary goal in designing an ISO is to have it cover a broad area. NSP witness Volkmann testified as follows:

Q. Do you have any examples where an ISO the size of MAPP would aid reliability of the MAPP transmission network?

A. Yes. On Sunday, May 19, 1996, a tornado took down several towers on the Prairie Island to Byron 345 kV line, a major facility in the exporting of energy from the Upper Midwest. NSP, in an anticipation of problems on Monday morning, had reduced a significant amount of its own transactions. On Monday morning regional transactions began and placed the western Wisconsin transmission system on the verge of voltage collapse and a service outage to the end use customers in Western Wisconsin. The NSP control center operator was able to arrest the voltage collapse by placing expensive, fast starting Wheaton generation on line. This action was and had to be taken before MAPP Line Loading Relief could be initiated to arrest the condition. The eventual Line Loading Relief action reduced more than 2,200 MWs of transactions to maintain the western Wisconsin system in a secure state. With an ISO the size of MAPP, the ISO would have recognized a system problem and refused to schedule 2,200 MWs of transactions on Sunday night and not have put the western Wisconsin system at risk on Monday morning. The ISO never would have waited until Monday morning to curtail 2,200 MWs.

With a MAPP-sized ISO, virtually all of the energy flowing on MAPP-WUMS interface would be under the control and authorization of the ISO, and a mechanism could exist to fairly and non-discriminatory charge the users of the system generation re-dispatch. However, an ISO the size of Primergy or the State of Wisconsin does not solve this problem.

NSP Ex. 12, pp. 9-10.

66. The details of ISO design will be dealt with in the pending FERC merger case and future ISO filings. Further, ISO design and operation will be subject to continuing regulatory oversight by FERC. The ALJ finds that it is not necessary for the Minnesota Commission to get into the level of detail which some of the parties have advocated. This proceeding is not necessarily the appropriate forum in which to resolve all questions surrounding appropriate ISO standards. As NSP states in its initial brief:

While the Minnesota PUC undoubtedly will want to be fully informed on the issues surrounding the inauguration of an ISO, it is not clear that the Commission has determined that it wants to establish its own set of ISO standards or render an independent judgment on each point and subpoint of ISO design. Neither of the

two issues encompassed in this segment of the hearings directly indicates that the Commission wanted parties to delve into the details of ISO design in this hearing. It may be that an ISO meeting the general FERC standards and any additional FERC requirements for the Primergy merger will be a sufficient condition in the context of this Minnesota case.

NSP Initial Brief at 23. OAG also implicitly recognizes that the Commission may not wish to delve into the fine points of ISO design.

67. The need for an ISO is not strictly a merger-related issue. An ideal ISO would cover a broad region encompassing many utility systems. MAPP recognizes the need for a regional ISO and has already established an ISO sub committee encompassing a broad range of interested stakeholders. DPS Ex. 20 at 16.

68. FERC and state regulatory commissions may approve a utility-specific ISO to mitigate potential market abuses from a merger. However, any utility-specific ISO is necessarily a second-best solution. The ultimate goal is a regional ISO that would supplant or absorb any less effective utility- or state-specific ISO approved in a merger proceeding. As WI witness Mr. Russell testified, imposition of different ISO requirements by the FERC, the Public Service Commission of Wisconsin and the Minnesota Public Utilities Commission could raise issues of preemption as well as delay or prevent merger implementation. Tr. 1 at pp. 48-49. He also acknowledged that it would be preferable to have a single plan for as large a region as possible. *Id.* at 50. Furthermore, Mr. Russell freely stated that he has no lack of confidence in the ability of FERC to ensure that an appropriate ISO is ordered in connection with the proposed merger. *Id.* at 51. FERC will no doubt render a decision on the Primergy ISO in its merger proceeding. Consequently, any ISO approved as a condition of the merger in this proceeding should avoid provisions that might not be applicable or appropriate for a larger, regional ISO, or conflict with conditions likely to be ordered by FERC.

69. Any ISO imposed as part of this merger should be sufficiently flexible that it can be incorporated into an effective regional ISO of the type which may well evolve from further FERC orders and proceedings and/or from the MAPP Regional Transmission Group (RTG). DPS Ex. 20 at 16-17. Restrictive provisions in any ISO proposal which would discourage prospective member utilities from joining should be avoided.

70. As the presiding federal ALJ reasonably concluded, this merger case is not the appropriate forum for determining the ultimate ISO model. This proceeding requires instead the more limited determination whether Applicants' ISO is capable of preventing Primergy from manipulating the transmission system to its advantage by virtue of the merger. Presiding Administrative Law Judge's Initial Decision, at 62-63. The federal ALJ concluded that Applicants' ISO, with modifications now incorporated therein, would prevent Primergy from manipulating transmission access from MAPP to

WUMS and from engaging in anti-competitive activity. Id. The undersigned ALJ agrees.

DISCUSSION

Wisconsin Intervenors spent most of their time and effort debating the details of an ISO. The record contains a detailed proposal from WI which, they claim, is needed to protect users of the interface from abuse. The undersigned ALJ cannot see the benefit of Minnesota designing a detailed ISO when we are not yet sure what the FERC Final Order will provide. Nor do we know what the State of Wisconsin will do. The primary beneficiaries of a strong ISO are the Wisconsin utilities and end-users. The Minnesota utilities appear to be satisfied with the Applicant's ISO and other commitments outlined in the preceding Findings. There is a legitimate concern that if Minnesota, Wisconsin and FERC get into a protracted debate about the best design for an ISO, we may end up with more than one ISO, or with one that does not satisfy the goal of including as many participants as possible. As witness Russell acknowledged, FERC would likely ultimately prevail, in terms of the ISO, but if one (or both) states conditioned their merger approvals on any detailed ISO other than the FERC-adopted ISO, the delays involved in resolving the matter could derail the merger.

CPA advocated for representation of G&T cooperatives on the ISO Board of Directors, as well as advocated for other mechanics of ISO governance. It is neither necessary nor appropriate to resolve such details at this stage.

At this stage, the question that needs to be answered is whether the public interest would be harmed by allowing the merger to proceed in light of the potential for abuse of the MAPP-WUMS interface. While the ISO is one important tool for preventing abuse, the commitments and institutional arrangements outlined in the preceding Findings, along with the Applicant's proposed ISO (which is only likely to be strengthened, not weakened, by FERC and Wisconsin), provide adequate safeguards for Minnesota. The total redesign and detailed "bullet proofing" advocated by WI is just not needed in order to answer the question that needs to be resolved at this point.

Impact on Other Minnesota Utilities

71. The Commission also asked parties to address the question of the possible impacts on other Minnesota utilities of any manipulation of the MAPP-WUMS interface by a merged NSP - Wisconsin Energy. The Commission expressly stated its concern that any such anti-competitive behavior could have a "resulting impact on other consumers in the upper Midwest, and particularly in Minnesota." June 25, 1996 Order Establishing Procedural Framework, p.15. Anticompetitive manipulation of the MAPP-WUMS interface would create negative long-term impacts on other Minnesota utilities, Minnesota ratepayers and the regional economy. However, the findings that Primergy will have neither the incentive or ability to use transmission ownership to restrict non-Primergy transactions renders the second question moot. If there will be no manipulation, there will be no adverse impacts on anyone, including other Minnesota utilities.

72. It is unlikely that any utility in Minnesota would be adversely affected by Primergy's ownership of the interface for two reasons. First, as discussed above, Primergy would be unable to manipulate the MAPP-WUMS interface for its own benefit. It is unlikely that Primergy would be able to constrain the MAPP-WUMS interface for its own benefit or to receive preferential treatment when the interface was constrained. This conclusion is based on the Findings above, which can be summarized by the following factors:

- Primergy's proposed equal open-access tariff, which meets the requirements of FERC Order No. 888;
- Primergy's establishment of an OASIS that meets the requirements of FERC Order No. 889;
- Primergy's proposed ISO; and
- the provisions in the MAPP Restated Agreement.

Therefore, other utilities in Minnesota would not be harmed by Primergy's ownership of the interface.

73. Second, and more significantly, none of the bulk-power utilities in Minnesota opposes the merger. While some Minnesota utilities initially expressed concerns about potential impacts of the Primergy merger on their operations, no Minnesota utility opposes the merger at this time. Minnesota Power Company, Dairyland Cooperative Power, Cooperative Power, United Power Association, Otter Tail Power, Minnesota Municipal Power Agency, Central Minnesota Municipal Power Authority and the Southern Minnesota Municipal Power Agency have all reached agreement with Primergy resolving all outstanding transmission issues. NSP has also reached agreement with several utilities in other states, including Wisconsin Public Power, Inc. (the complainant in Finding 34), WPS and Upper Peninsula Power Company. Only one Wisconsin utility, Madison Gas & Electric, still opposes approval of the merger. Interstate Power Company did not file any comments regarding transmission issues. The ALJ's understanding is that Interstate Power Company does not oppose the merger. DPS Ex. 19 at 20. The lack of any objection to the proposed merger by the Minnesota utilities is the strongest possible evidence that they no longer regard Primergy's ownership of the interface as a serious threat to themselves.

Based upon the above Findings of Fact, the Administrative Law Judge makes the following:

CONCLUSIONS

1. Based on Primergy's special commitments, FERC Order Nos. 888 and 889, Primergy's proposed ISO, and MAPP's Restated Agreement, the public interest will not be harmed by Primergy's ownership or control of the MAPP-WUMS interface.

2. The proposed merger will not provide Primergy with the ability or the incentive to negatively impact competition through manipulation of transfer capability through the MAPP/WUMS interface.

3. Based on the aforementioned factors and the agreements reached between Primergy and other utilities in Minnesota, Primergy's ownership or control of the interface would be unlikely to harm other utilities in Minnesota.

Dated this 7th day of February, 1997.

ALLAN W. KLEIN
Administrative Law Judge

Recorded: Transcript Prepared. Janet Shaddix & Associates. Two Volumes for this Segment.

MEMORANDUM

These Findings and Conclusions address only two of the five specific questions which the Commission referred to OAH for contested case proceedings. And those five questions form only part of the relevant inquiry the Commission must conduct in its review of this filing. No single issue in isolation can conclusively demonstrate that the merger is either consistent or inconsistent with the public interest. Ultimately, the Commission will need to consider all relevant factors in making that determination. Thus, the Administrative Law Judge makes no final recommendation regarding merger approval or denial.

AWK

^[1] The Motion to the ALJ was faxed to the ALJ on November 18. However, the transmission did not begin until after 4:30 p.m., and Minn. Rule pt. 1400.5100, subp. 9 sets 4:30 p.m. as the cutoff for timely filing by fax.

^[2] It must be understood that the capacity of the interface is a variable number that changes from instant to instant. The real world capacity of an interface which is part of a dynamic electric grid is impossible to measure with precision. While 700 MW can be used as a starting point for discussion, it must be understood to be only a starting point.

^[3] In the FERC proceeding, the concerns were presented by Attorney Lee Cullen on behalf of a coalition known as "Certain Intervenor" (CI). In Minnesota, Mr. Cullen represented "Wisconsin Intervenor" (WI). There is substantial overlap between the two groups and their concerns.